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BOEING
AIRPLANE COMPANY
and SUBSIDIARY COMPANIES



Report to Stockholders

Year Ended December 31, 1939

JOHN

WILLIAM COMPANY

NEW YORK

WILLIAM COMPANY

NEW YORK

ANNUAL REPORT

To the Stockholders of Boeing Airplane Company:

FINANCIAL STATEMENTS

THE statement of consolidated income and surplus of your Company and its subsidiary companies for the year 1939 and the consolidated balance sheet as of December 31, 1939, are submitted herewith, together with the report of Allen R. Smart & Co., independent certified public accountants.

The profit and loss statement shows a net loss of \$3,284,073.84 for the year 1939. Most of this loss has been occasioned by the excess of cost over sales price of the development and manufacture of four-engine flying boats (Clippers) for Pan American Airways, and four-engine transport aircraft generally referred to as "Stratoliners."

Under date of November 24, 1939, a letter was addressed to stockholders, setting forth the condition of your companies as of September 30, 1939. This report is primarily devoted to an account of the developments in your companies since that date. In our letter of November 24th we reported a net loss for the period from January 1, 1939, to September 30, 1939, of \$2,606,106. The loss for the period September 30th to December 31st, 1939, has been principally due to losses incurred on four-engine bombardment aircraft in the

amount of \$232,774.90, of which \$74,734.05 is reflected in an inventory reserve, and an increase in the estimated cost to complete the Stratoliners in the amount of \$368,580.58. In the case of the Stratoliners, this additional loss arose primarily because of modifications in these aircraft as a result of extensive flight tests conducted during the latter part of the year 1939. Increases in cost of the four-engine bombardment aircraft were largely due to rework and making up of shortages of parts and payments to labor for overtime necessary to meet delivery schedules.

OPERATING DIVISIONS

Your Company has one direct subsidiary, Boeing Aircraft Company, which is wholly owned. Boeing Aircraft Company, in turn, has one wholly owned subsidiary, Boeing Aircraft of Canada Limited. The plants of your Company and its subsidiaries are located as follows:

Boeing Aircraft Company.....	Seattle, Washington
Boeing Airplane Company, Stearman Division.....	Wichita, Kansas
Boeing Aircraft of Canada Limited.....	Vancouver, B. C.

DELIVERIES

During the last quarter of 1939 satisfactory progress was made in deliveries to the United States Army Air Corps of four-engine bombardment aircraft under a contract in the amount of \$9,928,895 entered into in August of 1937. No substantial deliveries were made prior to September, 1939, but thereafter and to March 1, 1940, approximately 75% of the total contract was completed and delivered. It is expected that the contract will be completed during the month of April, 1940.

All of the undelivered Stratoliners are under order for use by Pan American Airways and Transcontinental & Western Air, Inc. The first of these aircraft manufactured for delivery to Pan Ameri-

can Airways has been under test by the Civil Aeronautics Authority for a period of more than three months. A temporary certificate of air worthiness has been granted on this aircraft and it is expected that the final certificate will issue as soon as the engineering data has been reviewed by the Authority in Washington, D. C. This data is at present in its hands. It is expected that deliveries of all Stratoliners will be completed prior to July 1, 1940.

MANAGEMENT

The present management of your Company undertook its duties on September 9, 1939. It was considered of primary importance to readjust procedures so as to bring delivery schedules into line with contractual obligations. The progress made in this direction has been set forth above.

The Management is now engaged in a study of the production system and manufacturing processes of Boeing Aircraft Company with the view of increasing the efficiency of the Manufacturing Departments.

During the year 1939 important additions were made to the technical, aerodynamic and flight research departments and a new factory manager has been appointed.

ADDITIONAL PLANT FACILITIES

During December, 1939, Boeing Aircraft Company leased 165,000 additional square feet of factory space near the assembly plant in Seattle. Its occupancy has reduced the congestion in the other plants of the company. In the opinion of the management the acquisition of this necessary space through lease is to be preferred, under present conditions, to the construction of additional facilities.

The plant facilities of the Stearman Division have been increased by an addition of 36,500 square feet to the main building and by the erection of new buildings to house the heat treating, anodizing, forming and foundry units of the plant.

UNFILLED ORDERS

The unfilled orders of your Company and its subsidiaries as of various dates are shown below:

December 31, 1937.....	\$14,112,298
December 31, 1938.....	14,894,918
December 31, 1939.....	23,002,574

Current unfilled orders for military purposes include four-engine bombardment and single-engine primary training aircraft for the United States Army Air Corps. Training aircraft are also under order for the Governments of Cuba, Brazil and Venezuela. Commercial aircraft under order include six Clippers for use by Pan American Airways and eight Stratoliners, three of which will be delivered to Pan American Airways and the remainder to Transcontinental & Western Air, Inc. The unfilled orders also include approximately \$900,000 (Canadian dollars) representing the uncompleted portion of a contract between Boeing Aircraft of Canada Limited and the Dominion of Canada. With the exception of the Clippers and some of the single-engine primary training aircraft, all are expected to be completed during the year 1940.

In addition to the contract for four-engine bombardment aircraft previously mentioned, the unfilled orders include a further contract for aircraft of this type in the amount of \$8,426,190 entered into in September, 1939. The six Clippers under order are at prices substantially in excess of the prices obtained for the six Clippers delivered in 1939.

PROSPECTIVE BUSINESS

Your companies are actively engaged in seeking additional business. In view of conditions existing in Europe, this includes active sales effort in that market as well as the domestic one. An existing contract grants to the United States Army Air Corps certain options for purchase of four-engine bombardment aircraft and it is our opinion that a decision relative to the exercise of these options will be made in the near future.

BANK LOAN

In our letter of November 24, 1939, it was stated that application had been made for a bank loan of not to exceed \$5,500,000, in which the Reconstruction Finance Corporation had agreed to participate. Arrangements for this loan were completed in February, 1940, and as of March 1, 1940, Boeing Aircraft Company was indebted under the loan in the amount of \$4,740,000.00. This indebtedness is guaranteed by your Company and mortgages have been placed upon the plants, machinery, equipment and certain other property of your companies and the proceeds of aircraft contracts have been assigned.

INCREASED CAPITALIZATION

At a special stockholders' meeting held December 29, 1939, approval was given to the increase in capitalization of the Company from 800,000 shares to 1,250,000 shares. No definite program has been adopted by the Directors for the issuance of additional shares, but the Directors have under consideration an offer to stockholders of rights to subscribe at such time as conditions make such an offering advisable.

By Order of the Board of Directors.

P. G. JOHNSON,
President.

BOEING AIRPLANE COMPANY A

CONSOLIDATED B

December

ASSETS

CURRENT ASSETS:

Cash		\$ 241,144.26
Notes and Accounts Receivable:		
Trade Notes and Accounts Receivable.....	\$1,304,140.35	
Sundry Accounts and Accrued Interest.....	32,889.32	
	<u>\$1,337,029.67</u>	
Less—Reserve for Doubtful Accounts.....	1,399.17	1,335,630.50
Inventories:		
Contracts and work in process at the lower of cost or estimated proportionate sales value (Note 1):		
Work in process on certain sales contracts, including unprocessed materials, title to substantially all of which has passed to vendee—less progress payments of \$3,122,764.94 and reserve of \$74,734.05.....	\$2,879,261.13	
Other work in process—less reserve of \$1,945,565.94....	1,973,682.32	
Raw Materials and Finished Products (less reserve of \$3,921.67) at substantially the lower of cost or market	446,856.26	5,299,799.71
TOTAL CURRENT ASSETS.....		<u>\$6,876,574.47</u>

INVESTMENTS AND OTHER ASSETS:

Deposits with Mutual Insurance Companies.....	\$ 36,795.00	
Miscellaneous Stocks	4,640.00	41,435.00

FIXED ASSETS:

Property and Equipment, at Cost:		
Land and Buildings.....	\$1,822,681.26	
Machinery, Tools and Equipment.....	1,036,084.36	
	<u>\$2,858,765.62</u>	
Less—Reserve for Depreciation.....	878,734.83	
	<u>\$1,980,030.79</u>	
Land, Buildings and Equipment of Stearman Aircraft Division at reduced values, less reserve for depreciation of \$55,365.17	315,939.20	2,295,969.99

DEFERRED CHARGES:

Prepaid Rent	\$ 21,551.43	
Unexpired Insurance, etc.....	18,204.14	39,755.57
TOTAL ASSETS		<u>\$9,253,735.03</u>

NOTE: The above consolidated balance sheet is

AND SUBSIDIARY COMPANIES

BALANCE SHEET

31, 1939

LIABILITIES AND CAPITAL

CURRENT LIABILITIES:

Notes Payable to Banks (Note 2).....	\$3,601,565.67
Accounts Payable—Trade	696,288.95
Accrued Wages, Taxes, etc.....	645,984.99
Provision for Canadian Provincial Income Tax.....	32.61
Deposits on Sales Contracts.....	418,551.02
Deposit on Terminated Sales Contract Held to Secure Possible Damages	42,285.00
TOTAL CURRENT LIABILITIES.....	\$5,404,708.24

CAPITAL STOCK AND SURPLUS:

Capital Stock (Note 3):

Authorized 800,000 shares of \$5.00 par value

Issued and Outstanding 720,860 $\frac{3}{4}$ shares..... \$3,604,303.75

To be issued for shares of Capital Stock of United Aircraft & Transport Corporation upon presentation for exchange—1,097 $\frac{1}{4}$ shares.....

5,486.25

\$3,609,790.00

Paid-In Surplus

917,203.71

\$4,526,993.71

Earned Surplus (Deficit) Since September 30, 1939.....

677,966.92 3,849,026.79

TOTAL LIABILITIES AND CAPITAL.....

\$9,253,735.03

BOEING AIRPLANE COMPANY
AND SUBSIDIARY COMPANIES

Notes to Consolidated Balance Sheet

December 31, 1939

NOTE 1: Inventories of work in process on sales contracts, title to substantially all of which has passed to vendee (less reserve of \$74,734.05), are valued at the lower of cost or estimated proportionate sales value after transfer between certain contracts of \$248,616.73 as a prorated proportion of expenses of engineering, tooling, etc., and the inclusion of development expenses of \$55,474.65 (of which \$51,868.39 was deferred at December 31, 1938). Such total amount of \$304,091.38 is in the opinion of the management a part of the costs under a contract with the United States. Reference is made to Note 1 to the Consolidated Profit and Loss Statement.

Other work in process is valued at the lower of cost or estimated proportionate sales value. In the case of the four-engine transport project, costs to December 31, 1939, including \$329,335.46 deferred as development expenses as at December 31, 1938, were reduced to sales price less estimated cost to complete by means of a reserve of \$1,945,565.94 to eliminate to that extent from such costs the estimated development expenses, losses due to delays, changes, etc., pursuant to action taken by the Board of Directors. Reference is made to Note 3 to the Consolidated Profit and Loss Statement.

NOTE 2: On February 9, 1940, a subsidiary of the Company, as Borrower, delivered to The Pacific National Bank of Seattle, its promissory note in the amount of \$5,500,000.00 pursuant to which and under certain conditions amounts were to be advanced by the Bank to the Borrower from time to time. The first amount so advanced was applied in part to the payment of notes payable to banks at December 31, 1939, in the amount of \$3,400,000.00, upon which notes the Company and such subsidiary were jointly and severally liable. The indebtedness represented by said note is secured by a mortgage upon the real property, machinery, equipment, patents, trade marks, copyrights and certain other personal property of the Borrower. It is likewise secured by a pledge of stock of Boeing Aircraft of Canada Limited, and an assignment of the account receivable owing by that company to the Borrower. It is further secured by an assignment of the moneys due or to become due under substantially all of the contracts of the Borrower for the manufacture and sale of aircraft and parts therefor, and in the case of contracts with the United States, the Bank has authority to collect the payments due the Borrower under substantially all of such contracts. Payment of indebtedness represented by said note is unconditionally guaranteed by the Company, and, as security for the performance of such guaranty, the Company has mortgaged its real property, machinery, equipment, patents and certain other personal property and has assigned moneys due or to become due under substantially all of its contracts for the manufacture and sale of aircraft or parts therefor. In case of contracts of the Company with the United States, the Bank has power to collect the proceeds of substantially all of such contracts. The loan transaction above referred to was consummated in accordance with the provisions of a Loan Agreement dated December 26, 1939, and delivered February 7, 1940, between such subsidiary, the Company and said Bank, which Loan Agreement contains various covenants on the part of the subsidiary, the Company and the Bank.

The loan represented by said note was granted pursuant to the Application of the Borrower dated October 4, 1939, for Participation Loan under Section 5(d) of the Reconstruction Finance Corporation Act as amended.

NOTE 3: On December 29, 1939, the stockholders of the Company authorized an amendment to the Certificate of Incorporation increasing the authorized Capital Stock of the Company from 800,000 shares to 1,250,000 shares of \$5.00 par value. Such amendment became effective upon filing in the State of Delaware on January 15, 1940.

NOTE 4: The basis of converting the assets and liabilities of the Canadian subsidiary into U. S. Dollars at December 31, 1939, is as follows:

Current assets and current liabilities (in a net amount of \$109,729.97 U. S. Dollars) at the mean New York cable discount rate on that date;

Capital assets and related reserves on the basis of dollar for dollar.

Certain limitations have been placed on exchange withdrawals by the Dominion of Canada.

NOTE 5 CONTINGENT LIABILITIES:

(1) In respect of a further loss which it is estimated a subsidiary of the Company may incur subsequent to December 31, 1939, in the amount of \$37,221.27 upon completion of a certain contract in progress.

(2) With respect to pending claims and actions for alleged infringement of patents and other causes.

BOEING AIRPLANE COMPANY
AND SUBSIDIARY COMPANIES

Consolidated Profit and Loss Statement

Year ended December 31, 1939

GROSS SALES, LESS DISCOUNTS, RETURNS AND ALLOWANCES.....		\$11,846,893.56
COST OF SALES.....	\$11,731,877.11	
PROVISION TO REDUCE INVENTORY OF 1937 CONTRACT FOR FOUR-ENGINE BOMBARDMENT AIRCRAFT TO ESTIMATED PROPORTIONATE SALES VALUE (Note 1).....	74,734.05	
COSTS AND DEVELOPMENT ON FLYING BOATS IN EXCESS OF SALES PRICE (Note 2)	722,383.98	
EXCESS OF COSTS PLUS ESTIMATED COST TO COMPLETE OVER SALES PRICE ON FOUR-ENGINE TRANSPORTS (Note 3)	1,945,565.94	
ENGINEERING RESEARCH EXPENSES.....	81,230.72	
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	343,789.88	
PROVISION FOR DOUBTFUL ACCOUNTS....	804.81	
DEPRECIATION	141,341.82	15,041,728.31
OPERATING LOSS		\$ 3,194,834.75
OTHER INCOME:		
Discount on Purchases.....	\$ 27,005.43	
Royalty and License Fees.....	15,560.96	
Profit on Sale of Fixed Assets.....	17,314.35	
Profit on Sale of Real Estate Investment.....	3,301.99	
Interest Earned	1,375.93	
Sundry	2,854.12	67,412.78
		\$ 3,127,421.97
INCOME DEDUCTIONS:		
Interest Expense	\$ 76,925.68	
Losses on Crashed Aircraft, including Expenses in Connection Therewith.....	57,273.80	
Exchange Fluctuations	15,519.00	
Sundry	6,897.97	156,616.45
NET LOSS—Before Income Tax.....		\$ 3,284,038.42
PROVISION FOR CANADIAN PROVINCIAL INCOME TAX.....		35.42
NET LOSS FOR YEAR.....		\$ 3,284,073.84

NOTE: The above consolidated profit and loss statement is subject to the notes on the following page.

BOEING AIRPLANE COMPANY
AND SUBSIDIARY COMPANIES

Notes to Consolidated Profit and Loss Statement

Year ended December 31, 1939

NOTE 1: The amount of \$74,734.05 represents provision made to reduce the remaining inventory value of a contract entered into in 1937 for four-engine bombardment aircraft to estimated proportionate sales value thereof at December 31, 1939, after crediting thereto a prorated proportion of engineering, tooling, etc., in the amount of \$248,616.73.

NOTE 2: As at December 31, 1938, a subsidiary of the Company charged off \$488,068.14 as costs in excess of estimated proportionate sales price on six flying boats after deferring \$550,000.00 as development costs representing the amount which the subsidiary then expected to recover on future contracts and/or from sale of design rights.

The original six flying boats under contract were completed in 1939 and costs incurred in that year in excess of the proportionate sales price in the amount of \$172,383.98 were charged off together with the \$550,000.00 deferred in 1938 as development costs. These charges were made by order of the Board of Directors in view of the uncertainties with respect to further orders for flying boats or orders for design rights. An option was exercised for six additional flying boats under the original contract at a price believed to be favorable but no portion of the development cost has been deferred as applying to it.

NOTE 3: As at December 31, 1938, a subsidiary of the Company deferred as development expenses costs of \$329,335.46 necessary to reduce the inventory value of four-engine transports to the estimated proportionate sales value thereof. This amount together with similar costs incurred and losses sustained to December 31, 1939, has been estimated to be \$1,945,565.94 computed as the excess of costs (including development expenses and estimated cost to complete) over sales price. The foregoing total of \$1,945,565.94, was charged to profit and loss for the year ended December 31, 1939, pursuant to action taken by the Board of Directors in view of the fact that no sales of additional aircraft or design rights had been made, of the uncertainties with respect to future sales and of the extraordinary nature of these costs.

NOTE 4: The operations of the Canadian subsidiary have been converted on the basis of the average New York cable discount rates for the year based upon the assumption of a dollar for dollar rate prior to September 1, 1939.

BOEING AIRPLANE COMPANY
AND SUBSIDIARY COMPANIES

Consolidated Earned Surplus (Deficit) Account

Year ended December 31, 1939

DEFICIT—January 1, 1939.....		\$ 872,369.41
ADD:		
Net Loss for Year ended December 31, 1939	\$3,284,073.84	
Additional Federal Income and Undistributed Profits Taxes for Year 1937.....	1,166.97	3,285,240.81
		<u>\$4,157,610.22</u>
DEDUCT:		
Refund of Federal Income and Undistributed Profits Taxes for Year 1936.....	\$ 333.18	
Cancellation of portion of Reserve for Insurance established on the books of a subsidiary subsequent to date of acquisition. The subsidiary subsequent to 1935 has carried insurance with others.....	7,623.83	
Transfer from Paid-In Surplus account so as to eliminate the deficit accumulated to September 30, 1939, pursuant to resolution adopted by the Board of Directors on November 22, 1939, and approved by the Stockholders on December 29, 1939....	3,471,686.29	3,479,643.30
DEFICIT—December 31, 1939.....		<u><u>\$ 677,966.92</u></u>

Consolidated Paid-in Surplus Account

Year ended December 31, 1939

BALANCE—January 1, 1939.....		\$4,357,459.32
ADD:		
Cancellation of that portion of the Reserve for Insurance which was established on the books of a subsidiary prior to date of acquisition. The subsidiary subsequent to 1935 has carried insurance with others.....	\$19,297.51	
Cancellation of Reserve for Contingencies established on the books of a subsidiary prior to date of acquisition.....	12,133.17	31,430.68
		<u>\$4,388,890.00</u>
DEDUCT:		
Transfer to Earned Surplus (Deficit) account so as to eliminate the deficit accumulated to September 30, 1939, pursuant to resolution adopted by the Board of Directors on November 22, 1939, and approved by the Stockholders on December 29, 1939.....		3,471,686.29
BALANCE—December 31, 1939.....		<u><u>\$ 917,203.71</u></u>

AUDITOR'S CERTIFICATE

Boeing Airplane Company,
Seattle, Washington.

We have examined the consolidated balance sheet of Boeing Airplane Company and Subsidiary Companies as of December 31, 1939, and the consolidated statements of income and surplus for the year then ended, have reviewed the system of internal control and the accounting procedures of the companies and, without making a detailed audit of the transactions, have examined or tested accounting records of the companies and other supporting evidence, by methods and to the extent we deemed appropriate.

As at December 31, 1938, the Company deferred certain development costs in respect to flying boat and four-engine transport projects, but at that time did not adopt a definite amortization policy and the method of writing off such expenses was deferred until such time as reasonable ascertainment could be made as to probable total quantities of products to be sold and the probable amounts to be realized from sale of design rights. No additional sales of products or sales of design rights have been made (except for the exercise of an option for six additional flying boats), and in view of the uncertainties with respect to further orders the directors authorized the writing off to profit and loss of the amounts deferred in 1938, together with similar costs incurred and losses sustained in the current year. Further reference is made to the notes to the financial statements.

In the work in process inventories, a contract with the United States includes in costs certain development expenses deferred as at December 31, 1938, and a prorated proportion of engineering, tooling, etc., transferred from another contract in process. After this transfer the inventories of work in process were valued at the lower of cost or estimated proportionate sales value.

In our opinion, the accompanying consolidated balance sheet and related statements of income and surplus present fairly the consolidated position of Boeing Airplane Company and Subsidiary Companies at December 31, 1939, and the results of their operations for the year, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

ALLEN R. SMART & CO.

Seattle, Washington,
March 4, 1940.

BOARD OF DIRECTORS

WILLIAM M. ALLEN
Of Messrs. Todd, Holman, Sprague
& Allen

HAROLD E. BOWMAN
Secretary and Treasurer
Boeing Aircraft Company

DARRAH CORBET
Seattle, Washington

CLAIRE L. EGTVEDT
Chairman
Boeing Aircraft Company

FRED P. LAUDAN
Vice-President
Boeing Aircraft Company

ROBERT J. MINSHALL
Vice-President
Boeing Aircraft Company

PAUL PIGOTT
Seattle, Washington

DIETRICH SCHMITZ
Seattle, Washington

P. G. JOHNSON
President and General Manager
Boeing Aircraft Company

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CLAIRE L. EGTVEDT.....*Chairman*
J. EARL SCHAEFER.....*Vice-President*
JAMES P. MURRAY.....*Vice-President*
HAROLD E. BOWMAN.....*Secretary and Treasurer*

General Counsel
TODD, HOLMAN, SPRAGUE & ALLEN

General Auditors
ALLEN R. SMART & CO.

Transfer Agent
CITY BANK FARMERS TRUST COMPANY, NEW YORK

Registrar
THE NATIONAL CITY BANK OF NEW YORK, NEW YORK

